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## **Thawing the Freeze: Cutting Costs and Increasing Efficiency by Granting Administrative Expense Priority to Nonquantifiable Benefits**

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# THAWING THE FREEZE: CUTTING COSTS AND INCREASING EFFICIENCY BY GRANTING ADMINISTRATIVE EXPENSE PRIORITY TO NONQUANTIFIABLE BENEFITS

## ABSTRACT

*Disputes over priority claims in bankruptcy proceedings are common because they are often the only way to recover assets from the limited pool available to claimants. Claims for professional fees for those who facilitate bankruptcy proceedings after the petition has been filed are given high priority to ensure that they have incentive to complete their work. However, those who come into bankruptcy with claims against the debtor have a much harder time recovering their costs if they do any work to assist with the proceedings. Currently, the administrative expense analysis requires these applicants to demonstrate that they made a substantial contribution to the estate before receiving priority on their claims for reimbursement. Courts overwhelmingly deny requests for administrative expenses under § 503 of the Bankruptcy Code because the applicant did not make a quantifiable benefit to the estate.*

*This Comment calls upon the Federal Judiciary and Congress to allow administrative expense priority for reasonable expenses to applicants who benefit the estate without being duplicative, self-interested, or meritless, but are unable to directly quantify how they did so. For applicants and their attorneys, this Comment serves as a guide on requesting administrative expense priority for costs incurred when a direct benefit cannot be shown.*

*The current substantial contribution analysis will be discussed to show why it should not require a benefit to be quantifiable. First, the types of potential applicants for this priority claim will be analyzed to demonstrate how each can benefit the estate in ways that are not quantifiable under the current interpretation of § 503(b)(3)(D). The language that courts commonly use to convey the rationale of a substantial contribution analysis will be discussed to show that precedent does not preclude the proposed interpretation. An interpretation is provided for the existing text of § 503(b)(3)(D) that would allow courts to make this change on a case by case basis. Finally, a change to the text of § 503(b)(3)(D) that would allow Congress to implement this change directly is provided as a model.*

## INTRODUCTION

Bankruptcy estates, by definition, do not have enough assets to cover all debts and expenses.<sup>1</sup> As a result, costs are prioritized by § 507 of the Bankruptcy Code (Code) to ensure that the assets of the estate are distributed in order of importance.<sup>2</sup> First priority is given to the repayment of professionals that facilitate proceedings because their work is essential for the debtor to make it through bankruptcy quickly and efficiently.<sup>3</sup> These highly prioritized repayments are classified as “administrative expenses” and they ensure that those who keep the estate running smoothly are not discouraged from participating due to a fear of not receiving payment.<sup>4</sup>

Other administrative expenses, however, are given second priority by § 507.<sup>5</sup> These include the costs incurred by a variety of interested parties: creditors,<sup>6</sup> indenture trustees,<sup>7</sup> equity security holders,<sup>8</sup> and committees representing creditors or equity security holders.<sup>9</sup> This group will be collectively referred to as “applicants” below. Those who qualify as applicants under § 503(b)(3)(D) only receive repayment if they show that their expenses were

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<sup>1</sup> An estate with sufficient assets to cover all expenses would have no use for discharge and would have no reason to enter the bankruptcy process.

<sup>2</sup> 11 U.S.C. § 507(a) (2019).

<sup>3</sup> *In re Goody's Family Clothing, Inc.*, 401 B.R. 656, 662 (D. Del. 2009).

<sup>4</sup> H.R. REP. NO. 95-595, at 186–87 (1977).

<sup>5</sup> 11 U.S.C. § 507(a)(2) (2019).

<sup>6</sup> A creditor is defined as an “entity that has a claim against the debtor that arose at the time of or before the order for relief concerning the debtor” by 11 U.S.C. § 101(10)(A) (2019). Entities with claims against the estate of a kind specified in 11 U.S.C. §§ 348(d), 502(f), 502(g), 502(h) or 502(i). Community claims are also creditors under 11 U.S.C. § 101(10).

<sup>7</sup> An “indenture trustee” is “the person or institution charged with the fiduciary duty of carrying out the terms of an agreement under which bonds or debentures are issued[.]” Mark A. Cohen, *Reimbursement of Indenture Trustees for Substantial Contribution Under Section 503 of the Bankruptcy Code*, 59 FORDHAM L. REV. 647 (1991) (citing [Bankruptcy Reform] Act of Nov. 6, 1978, Pub. L. No. 95-598, 92 Stat. 2549 (codified as amended at 11 U.S.C. §§ 101–1330 (1988))). The term indenture is defined as “mortgage, deed of trust, or indenture, under which there is outstanding a security, other than a voting-trust certificate, constituting a claim against the debtor, a claim secured by a lien on any of the debtor’s property, or an equity security of the debtor.” 11 U.S.C. § 101(28) (2019). The term indenture trustee is defined as a “trustee under an indenture.” 11 U.S.C. § 101(29) (2019).

<sup>8</sup> Under 11 U.S.C. § 101(16) (2019), the term “equity security” means “(A) share in a corporation, whether or not transferable or denominated ‘stock’, or similar security; (B) interest of a limited partner in a limited partnership; or (C) warrant or right, other than a right to convert, to purchase, sell, or subscribe to a share, security, or interest of a kind specified in subparagraph (A) or (B) of this paragraph.” The term “Equity Security Holder” is defined as the “holder of an equity security of the debtor” by 11 U.S.C. § 101(17) (2019).

<sup>9</sup> Committees representing creditors and equity security holders can apply for administrative expense reimbursement under the same provision as the parties they are representing. 11 U.S.C. § 503(b)(3)(D). However, this section does not allow for the repayment of administrative expenses for committees created under 11 U.S.C. § 1102, which use a different standard for reimbursement under 11 U.S.C. § 503(b)(3)(F).

“actual and necessary” and incurred while making a “substantial contribution” to the estate.<sup>10</sup>

This approach, although reasonable on the surface, has caused an unnecessary problem within bankruptcy litigation: the “substantial contribution” analysis has been interpreted to only allow administrative expense priority for claimants who can show that they made a benefit to a bankruptcy estate that is “quantifiable,” meaning that the benefit must be measurable and have directly contributed assets to the bankruptcy estate.<sup>11</sup> However, significant benefits can be conferred that are difficult or impossible to quantify under this standard.

The substantial contribution analysis in *Matter of D’Lites* provides a good illustration of what is not considered a quantifiable benefit under the current standard.<sup>12</sup> In *Matter of D’Lites*, the applicant, Walton Investments, Inc., ran the debtor’s business using Walton employees in an attempt to keep the company afloat.<sup>13</sup> Although this provided the estate with the benefit of a workforce that operated the business as it wound down, the court held that it did not constitute a substantial benefit to the estate in part because it could not be quantified.<sup>14</sup>

The court then compared the facts with those of a case heard by the Seventh Circuit Court of Appeals.<sup>15</sup> In *Park Terrace Townhouses v. Wilds*, the applicant “instituted a marketing program which significantly increased occupancy rates and monthly income” at the debtor’s property.<sup>16</sup> While the applicants in both cases made an effort to benefit the estate, only the applicant in *Park Terrace* was awarded administrative expenses because he was able to quantify the benefit he conferred.<sup>17</sup> This Comment proposes that an applicant who is unable to directly quantify a benefit to the estate should be granted administrative expense priority for reasonable expenses spent on good faith efforts to increase the value of the estate.

The proposed increase in the number of applicants who qualify for administrative expenses must be reconciled with the purpose of limiting priority in the first place. There are many reasons for having limits imposed on the range

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<sup>10</sup> 11 U.S.C. § 503(b)(3) (2019).

<sup>11</sup> See *In re D’Lites of Am., Inc.*, 108 B.R. 352, 356 (Bankr. N.D. Ga. 1989) (“[Applicant] insists that the continued operation of the business increased the value of D’Lites assets at the time of sale, but it does not quantify the benefit to the estate.”).

<sup>12</sup> *Id.*

<sup>13</sup> *Id.* at 354 (citing *Park Terrace Townhouses v. Wilds*, 852 F.2d 1019 (7th Cir. 1988)).

<sup>14</sup> *In re D’Lites of Am. Inc.*, 108 B.R. at 356.

<sup>15</sup> *Park Terrace Townhouses*, 852 F.2d 1019.

<sup>16</sup> *In re D’Lites of Am. Inc.*, 108 B.R. at 356 (citing *Park Terrace Townhouses*, 852 F.2d 1019).

<sup>17</sup> *Park Terrace Townhouses*, 852 F.2d at 1023.

of possible claims against the bankruptcy estate: § 503 is intended to balance competing interests in this context—on the one hand, promoting meaningful creditor participation—on the other hand, minimizing costs to the estate.<sup>18</sup> Therefore, courts have an interest in preventing administrative costs from “mushrooming,”<sup>19</sup> and excluding claims that are “duplicative,”<sup>20</sup> solely motivated by self-interest,<sup>21</sup> or create meritless legal actions.<sup>22</sup>

It is possible to recognize and endorse the restrictions above and still permit non-quantifiable benefits to a bankruptcy estate to be honored and repaid. When creditor participation can be encouraged while lowering costs to the estate, both aims of § 503 can be met simultaneously. Creditors who benefit the estate in ways that smooth the bankruptcy process, lower costs, foster collaboration, etc. should have the opportunity to recover reasonable costs for their efforts.

The current requirement that a benefit be quantifiable before priority is granted is problematic because it does not give applicants an incentive to assist in the administrative process. Instead, applicants face a “chilling effect”<sup>23</sup> because they are afraid to “throw good money after bad.”<sup>24</sup> With a small and manageable change in this area of the law, however, this problem can be eliminated without significant additional burdens being imposed on the bankruptcy process.

This Comment proposes a solution that requires only a small adjustment in the language or interpretation of § 503(b)(3)(D) but will result in increased judicial efficiency, shortened cases, and the more efficient use of resources. Allowing applicants to show that they benefited the estate in new ways will keep the competing interests of § 503 balanced<sup>25</sup> because not only will more

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<sup>18</sup> H.R. REP. NO. 95-595, at 186–87 (1977).

<sup>19</sup> See *In re Alert Holdings Inc.*, 157 B.R. 753, 757 (Bankr. S.D.N.Y. 1993) (citing *In re S & Y Enterprises, LLC*, 480 B.R. 452, 459 (Bankr. E.D.N.Y. 2012)); *In re Am. Plumbing & Mech., Inc.*, 327 B.R. 273, 279 (Bankr. W.D. Tex. 2005) (citing *In re Alert Holdings Inc.*, 157 B.R. at 757) (suggesting that if the court is not careful, administrative expense claims could eat up more and more assets of an estate until there is nothing left for creditors).

<sup>20</sup> See *In re D’Lites of Am., Inc.*, 108 B.R. 352.

<sup>21</sup> See *id.*

<sup>22</sup> See *In re Consol. Bancshares, Inc.*, 785 F.2d 1249 (5th Cir. 1986).

<sup>23</sup> “In addition to their own expenses, creditors may owe compensation and expenses to attorneys and accountants they have hired to facilitate workable solutions to reorganization. The prospect of paying expenses without reimbursement is daunting when one considers that most creditors ultimately will collect mere pennies on the dollar.” Edward A. Stone, *Encouraging Creditor Participation: Integrating the Allowance of Administrative Expenses with the Common Fund Theory*, 15 BANKR. DEV. J. 223, 223 (1998).

<sup>24</sup> Stephen A. Stripp, *An Analysis of the Role of the Bankruptcy Judge and the Use of Judicial Time*, 23 SETON HALL L. REV. 1329, 1393 (1993) (citing H.R. REP. NO. 95-595, at 92 (1977)).

<sup>25</sup> See *Leidos Eng’g, LLC v. Kior, Inc.* (*In re Kior, Inc.*), 567 B.R. 451, 459 (D. Del. 2017).

applicants have an incentive to participate in proceedings, but costs of administering the estate will decrease as well.

This Comment calls upon the Federal Judiciary and Congress to allow administrative expense priority for reasonable expenses to applicants who benefit the estate without being duplicative, self-interested, or meritless but are unable to directly quantify how they did so. For applicants and their attorneys, the following serves as a guide on requesting administrative expense priority for costs incurred when a direct benefit cannot be shown.

The current substantial contribution analysis will be discussed to show why it should not require a benefit to be quantifiable. First, the types of potential applicants for this priority claim will be analyzed to demonstrate how each can benefit the estate in ways that are not quantifiable under the current interpretation of § 503(b)(3)(D). The language that courts commonly use to convey the rationale of a substantial contribution analysis will be discussed to show that precedent does not preclude the proposed interpretation. An interpretation is provided for the existing text of § 503(b)(3)(D) that would allow courts to make this change on a case-by-case basis. Finally, a change to the text of § 503(b)(3)(D) that would allow Congress to implement this change directly is provided as a model.

#### *A. Participation is Worth Promoting*

This Comment does not suggest that courts should allow administrative expenses to all applicants, as this would almost certainly lead to estates being bombarded with frivolous claims. Instead, it proposes that judges read § 503(b)(3)(D) to allow for reasonable compensation for applicants who benefit the estate in a manner that cannot be quantified to an exact figure. The small amount of time spent working out how much an applicant has benefited the estate will be offset by the benefits of having more efficient parties take on administrative tasks. Creating new avenues for applicants to receive administrative expense priority will also incentivize behavior that adds value to the estate indirectly.

Providing applicants an incentive to benefit the estate will result in faster cases, larger recoveries, and more debtors exiting bankruptcy without being liquidated.<sup>26</sup> When applicants are in a better position to facilitate bankruptcy

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<sup>26</sup> Karen Gross & Patricia Redmond, *In Defense of Debtor Exclusivity: Assessing Four of the 1994 Amendments to the Bankruptcy Code*, 69 AM. BANKR. L.J. 287, 308 (1995) (discussing the promotion of creditor participation specifically but the concept applies to all types of applicants).

proceedings, they should not be encouraged to do so in exchange for nothing. Applicants should be given an incentive to participate, especially when doing so will reduce costs and increase efficiency. Preventing an applicant from receiving fair pay for work done reduces the efficiency of the bankruptcy system and overall participation.

While applicants are eligible for administrative expenses under the current interpretation of the law, it is rare that they will be reimbursed unless they demonstrate a quantifiable benefit to the estate. By allowing for new ways of showing how an applicant benefited the estate, the bankruptcy system will ensure that tasks are being completed by the most willing and capable party.

*B. Section 503(b)(3) is Drafted Ambiguously, Leaving Room for Courts to Implement this Solution Without Overturning Precedent*

The Code's administrative expenses statute, 11 U.S.C. § 503, provides in relevant part:

(b) After notice and a hearing, there shall be allowed administrative expenses, other than claims allowed under section 502(f) of this title, including . . . (3) the actual, necessary expenses, other than compensation and reimbursement specified in paragraph (4) of this subsection, incurred by . . . (D) a creditor, an indenture trustee, an equity security holder, or a committee representing creditors or equity security holders other than a committee appointed under section 1102 of this title, in making a substantial contribution in a case under chapter 9 or 11 of this title.<sup>27</sup>

Subsection D outlines the types of applicants that are eligible to receive administrative expenses under the § 503(b)(3)(D) analysis. Each potential applicant has a different route to be granted a substantial contribution. Each category of applicant is discussed below.

*C. The Solution Proposed by this Comment Applies to any § 503(b)(3)(D) Applicant*

Administrative expenses may be granted for four types of applicants who have made a "substantial contribution" to a bankruptcy estate under 11 U.S.C. § 503(b)(3)(D). Applicants may include: creditors,<sup>28</sup> indenture trustees,<sup>29</sup> equity

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<sup>27</sup> 11 U.S.C. § 503(b)(3)(D) (2019).

<sup>28</sup> See *supra* note 6.

<sup>29</sup> See *supra* note 7.

security holders,<sup>30</sup> and committees representing creditors or equity security holders.<sup>31</sup> Such administrative expenses receive increased priority to “encourage applicants to participate in the liquidation or reorganization of the estate.”<sup>32</sup> However, this goal is in direct tension with the “contrasting policy that administrative expenses of the estate be kept to a minimum.”<sup>33</sup> As a result, Section 503(b)(3)(D) is narrowly construed to provide expenses only when the applicant is found to have made a “substantial contribution” to the estate.<sup>34</sup>

Rather than suggesting that the substantial contribution requirement be removed from Section 503(b)(3)(D), this Comment suggests expanding the requirement slightly to include contributions that may not be able to be quantified to an exact figure.

Currently, the substantial contribution analysis limits the benefits that courts are willing to consider for administrative expenses to those that directly add quantifiable funds to the bankruptcy estate. Adding resources is just one of the many ways that an applicant can provide a benefit to the estate. The numerous other ways for applicants to benefit the estate should be promoted through the through the reward of administrative expenses.

Many of these benefits can be provided by any of the four applicant types. Any applicant could resolve an ambiguity in a case such as determining the proper value of a disputed item. Any applicant could allow the estate to continue operating as usual.<sup>35</sup> Any applicant could help draft and confirm a plan submitted by the debtor<sup>36</sup> or propose a plan that is confirmed when the debtor has failed to do so.<sup>37</sup> The temperature of a case could be “cooled off” by any applicant who “prevent[s] excess[] litigation and encourages[es] cooperation.”<sup>38</sup> Even urging for the appointment of a trustee can confer a benefit upon the estate.<sup>39</sup>

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<sup>30</sup> See *supra* note 8.

<sup>31</sup> See *supra* note 9.

<sup>32</sup> H.R. REP. NO. 95-595, at 186–87 (1977).

<sup>33</sup> *In re U.S. Lines, Inc.*, 103 B.R. 427, 429 (Bankr. S.D.N.Y. 1989).

<sup>34</sup> 11 U.S.C. § 503(b)(3)(D) (2019).

<sup>35</sup> *In re Am. Plumbing & Mech., Inc.*, 327 B.R. 273, 282 (Bankr. W.D. Tex. 2005) (citing *In re TransAmerican Natural Gas Corp.*, 978 F.2d 1409, 1420 (5th Cir. 1992)).

<sup>36</sup> *Id.* (citing *In re Richton Int'l Corp.*, 15 B.R. 854, 856 (Bankr. S.D.N.Y. 1981)); *In re Baldwin–United Corp.*, 79 B.R. 321, 340–41 (Bankr. S.D. Ohio 1987)).

<sup>37</sup> *In re Am. Plumbing & Mech., Inc.*, 327 B.R. at 282 (citing *In re Jelinek*, 153 B.R. 279, 281 (Bankr. D.N.D. 1993)).

<sup>38</sup> *Id.* (citing *Matter of Baldwin–United Corp.*, 79 B.R. 321, 343 (Bankr. S.D. Ohio 1987)).

<sup>39</sup> *Id.* (citing *In re Paolino*, 71 B.R. 576, 580 (Bankr. E.D. Pa. 1987)).



### 1. Creditors

Creditors have many ways to participate in bankruptcy proceedings that confer a benefit to the estate that are not quantifiable. There are several examples of courts finding that a creditor's nonquantifiable benefit constituted a substantial contribution in a Comment previously published in this journal: *Encouraging Creditor Participation: Integrating the Allowance of Administrative Expenses with the Common Fund Theory*.<sup>40</sup>

Creditors are often in a good position to detect fraud and bring it to the debtor's attention. "The Fifth Circuit held that causing a debtor to change its reorganization plan and recovering a fraudulent transfer that resulted in a \$3 million increase in the value of the property of the estate was a substantial contribution to reorganization."<sup>41</sup>

Creditors are familiar with inside information that can be helpful to determine logistical problems with litigation. "One creditors' committee attorney successfully prevented a debtor from retaining counsel with a conflict of interest problem, potentially saving the estate unnecessary expenses, and the court held this constituted a substantial contribution to the estate which entitled the creditor to reimbursement."<sup>42</sup>

Creditors can play an active role in the confirmation of a reorganization plan, cutting costs and reducing wasted time in the process. "Another bankruptcy court found a substantial contribution when an applicant's efforts resulted in the successful confirmation of a plan which provided for full payment to all creditors over the Debtor's proposed plan which provided for picayune or token payments . . . ."<sup>43</sup>

This Comment proposes that the many nonquantifiable benefits conferred by creditors should be considered a substantial contribution and granted administrative expense priority.

Creditors are in a difficult situation from the outset of a bankruptcy case because they are seeking recovery of debts owed to them by the debtor.<sup>44</sup> To make matters worse, creditors must use their own resources to participate in the

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<sup>40</sup> Stone, *supra* note 23.

<sup>41</sup> *Id.* (citing *In re DP Partners, Ltd.*, 106 F.3d 667, 673 (5th Cir. 1997)).

<sup>42</sup> *Id.* (citing *In re Envirodyne Indus., Inc.*, 176 B.R. 815, 820 (Bankr. N.D. Ill. 1995)).

<sup>43</sup> *Id.* (citing *In re 9085 E. Mineral Office Bldg., Ltd.*, 119 B.R. 246, 252 (Bankr. D. Colo. 1990)) (internal quotation omitted).

<sup>44</sup> *See id.* at 223.

proceedings and can be reluctant to “throw good money after bad.”<sup>45</sup> As a result, “[d]enying administrative expense priority to creditors who have out of pocket expenses creates a potentially chilling effect on creditor participation in the reorganization process.”<sup>46</sup> According to U.S. Trustee William Neary, promoting creditor participation in bankruptcy “would be well worth the effort; cases could move faster, creditor recoveries could be increased and a larger number of debtors might be salvaged.”<sup>47</sup>

## 2. Indenture Trustees

An indenture trustee is like a stakeholder whose duties and obligations are exclusively defined by the terms of an indenture agreement.<sup>48</sup> An “indenture agreement” is a contract made between a trustee and a bondholder that represents the bondholders’ interests.<sup>49</sup> This agreement also includes the rules and responsibilities of the parties.<sup>50</sup>

An indenture is a type of interest that a party may have that is defined by a contract made between a bond issuer and a trustee that represents the bondholder’s interests. The indenture trustee represents those interests by highlighting the rules and responsibilities of the parties.

An indenture is a mortgage, deed of trust, or similar, under which there is an outstanding security constituting a claim against the debtor, a security interest in the debtor’s property, or an equity security of the debtor.

Indenture trustees are individuals or institutions charged with the fiduciary duty of carrying out the terms of the contract between the bond issuer and bond holder.<sup>51</sup> The term “debentures” may also be used, but “[n]o formal legal distinction has developed concerning the terms ‘bonds’ and ‘debentures,’ but ‘bonds’ generally refers to secured long-term debt obligations, and ‘debentures’ to unsecured long-term debt obligations.”<sup>52</sup>

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<sup>45</sup> Stripp, *supra* note 24, at 1340 n.25 (citing H.R. REP. NO. 95-595, at 186–87 (1977)).

<sup>46</sup> Stone, *supra* note 23, at 223.

<sup>47</sup> Gross & Richmond, *supra* note 26, at 308.

<sup>48</sup> Hazzard v. Chase National Bank, 26 N.E.2d 801 (N.Y. 1940).

<sup>49</sup> See Stewart M. Robertson, *Debenture Holders and the Indenture Trustee: Controlling Managerial Discretion in the Solvent Enterprise*, 11 HARV. J.L. & PUB. POL’Y 461 (1988).

<sup>50</sup> See *id.*

<sup>51</sup> Cohen, *supra* note 7 (citing [Bankruptcy Reform] Act of Nov. 6, 1978, Pub. L. No. 95-598, 92 Stat. 2549).

<sup>52</sup> Robertson, *supra* note 49, at 461 n.2.

Indenture trustees become a part of the reorganization process when the debtor defaults on its obligations according to the Trust Indenture Act of 1939.<sup>53</sup> The Trust Indenture Act was created after the financial collapse of 1929 “to account for what in many cases appeared to be its flagrant disrespect for the rights of security holders prior to and during the administration of default proceedings.”<sup>54</sup>

Indenture trustees should be encouraged to meaningfully participate in the bankruptcy process because they often play a significant role in the confirmation or opposition of the reorganization plan.<sup>55</sup> Congress has specifically outlined that assisting the confirmation of a reorganization plan is sufficient grounds for a finding of a substantial contribution.<sup>56</sup> Furthermore, “Congress acknowledged that indenture trustees benefit the reorganization of an estate by their very participation under fiduciary standards.”<sup>57</sup>

Indenture trustees often play “a significant role in the initiation of the proceeding,”<sup>58</sup> as well as in the formulation of, opposition to or confirmation of the debtor’s plan of reorganization.”<sup>59</sup> As the confirmation or denial of the reorganization plan can make the difference between a debtor surviving a bankruptcy or being liquidated through chapter 7, indenture trustees are often in a position to make a substantial contribution to the estate. However, these contributions are currently being precluded from administrative expense priority because they are nonquantifiable.<sup>60</sup>

### 3. *Equity Security Holders*

Equity security holders hold some equity interest of the debtor in a bankruptcy case. Equity security or equity interest can include shares of a corporation or an interest of a limited partner in a limited partnership. It can also include the right to buy, sell, or subscribe to a share in a corporation or partnership. These individuals or entities may vote on a plan of reorganization

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<sup>53</sup> See 15 U.S.C. §§ 77aa–77rrr (1988).

<sup>54</sup> Robertson, *supra* note 49, at 461 n.2.

<sup>55</sup> Cohen, *supra* note 7 (citing 11 U.S.C. § 303(b) (1988)).

<sup>56</sup> See S. REP. NO. 95-598, at 66–67 (1978).

<sup>57</sup> *In re Multiponics, Inc.*, 436 F. Supp. 1072, 1076 (E.D. La. 1977) (discussing expenses being granted under Section 242 of the Code).

<sup>58</sup> Cohen, *supra* note 7, at 647 (citing 11 U.S.C. § 303(b) (1988)).

<sup>59</sup> *Id.* (citing H.R. REP. NO. 95-595, at 186–87 (1977)).

<sup>60</sup> A useful guide on how substantial contribution claims by indenture trustees should be treated is outlined by Cohen *supra* note 7, at 674.

and may file a proof of interest. Like other applicants, they hope to recover their interest in the bankruptcy estate.

Equity security holders can substantially contribute to the estate without it being quantifiable in much the same way that creditors can. The ability to take part in the reorganization vote alone makes them candidates for administrative expense priority because they can facilitate that process and substantially benefit the estate.<sup>61</sup>

#### 4. *Committees Representing Creditors or Equity Security Holders*

Groups of creditors and equity security holders can be represented by committees. These committees can benefit the estate in the same manner as the parties they represent. Official committees are regulated by the Code and often directly participate in chapter 11 reorganization plans. Courts are split on the issue of allowing official committees to be reimbursed for their costs and expenses incurred in making a substantial contribution.<sup>62</sup> Unofficial or ad hoc committees are not regulated and act just as a group of creditors or equity security holders would.

Courts have held that official committees appointed under chapter 11 are entitled to administrative expenses because of implied authority. Other courts “presume” that expenses from official committees are reimbursable.<sup>63</sup> However, official committees have been totally precluded from receiving administrative expenses from still other courts.<sup>64</sup> Those courts preclude official committees from recovering under § 503(b)(3)(D) because they are already granted attorney’s fees and expenses statutorily.<sup>65</sup>

Although this discussion is outside the scope of this Comment, the principle that any applicant who provides a substantial contribution to the estate should be granted an administrative expense does include official committees.

Committees may substantially contribute to the estate just as their individual members would, but often do so on a larger scale. In practice, a substantial contribution was found when an attorney representing a creditors’ committee

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<sup>61</sup> See S. REP. NO. 95-598, at 66–67 (1978).

<sup>62</sup> Compare *In re Grynberg*, 19 B.R. 621, 622–23 (Bankr. D. Colo. 1982), with *In re Major Dynamics, Inc.*, 16 B.R. 279, 280 (Bankr. S.D. Cal. 1981).

<sup>63</sup> *In re Western Co. of North America*, 123 B.R. 546 (N.D. Tex. 1991).

<sup>64</sup> *In re Auto. Nat’l Brands, Inc.*, 65 B.R. 412 (Bankr. W.D. Pa. 1986).

<sup>65</sup> *Id.* at 415.

prevented a debtor from retaining counsel that would have created a conflict of interest in the proceedings that could cost the estate unnecessary expenses.<sup>66</sup>

Each of the four types of applicant can substantially contribute to the estate without having that contribution be quantifiable. When conducting the substantial contribution analysis, the language used by courts does not require the benefit be quantifiable, so applicants should not be denied recovery on that ground.

*D. All Applicants Should Have the Opportunity to Recover Reasonable Expenses Incurred to Indirectly Benefit the Estate*

Nonquantifiable benefits should not be automatically excluded from the substantial contribution analysis solely because they cannot be quantified. Maximizing the estate's assets<sup>67</sup> without directly adding funds still benefits the bottom line. Expediting the case<sup>68</sup> reduces all expenses and allows all creditors to receive payment in less time. Implementing an incentive plan is often more easily accomplished by an applicant than by a debtor,<sup>69</sup> saving time and money for the estate. An applicant cooperating with creditors can also provide major benefits to the estate without directly increasing its assets.<sup>70</sup> Negotiating the resolution of the confirmation hearing is a major challenge for debtors and is often only possible through the efforts of applicants.<sup>71</sup>

While it is currently unusual for applicants to confer a benefit upon the estate, providing additional methods of securing administrative expense priority would incentivize this in the future. Most applicants cannot risk investing time and effort into increasing the value of an estate when they are overwhelmingly denied recovery. This Comment proposes that applicants should not be automatically excluded from administrative expense priority because no direct benefit to the estate can be shown. Instead, courts should allow applicants to demonstrate how their efforts conferred a benefit upon the estate indirectly and grant administrative expense priority to those who can show such benefit.

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<sup>66</sup> Stone, *supra* note 23, at 227 (citing *In re Envirodyne Indus., Inc.*, 176 B.R. 815, 820 (Bankr. N.D. Ill. 1995)).

<sup>67</sup> *Id.* at 248.

<sup>68</sup> Gross & Redmond, *supra* note 26, at 308 (trustee Neary argues that increasing creditor participation will lead to, among other benefits, faster case administration).

<sup>69</sup> Rebecca Revich, *The KERP Revolution*, 81 AM. BANKR. L.J. 87 (2007).

<sup>70</sup> Stone, *supra* note 23, at 233.

<sup>71</sup> *Steere v. Baldwin Locomotive Works*, 98 F.2d 889, 891 (3d Cir. 1938) (assisting with the confirmation plan has been seen as a benefit to the estate for almost 100 years).

This solution does leave open another ambiguity that must be addressed. To compensate an applicant for conferring a benefit upon the estate that cannot be quantified, the value of that compensation must be determined. This Comment proposes that courts should grant administrative expense priority to applicants for reasonable costs incurred while making a good faith effort to benefit the estate. These indirect benefits should result in compensation even if they appear to result in a net monetary loss for the estate. Costing the estate money in one area while saving it more money in another can easily result in a significant benefit for the estate.

When an applicant acts in good faith to benefit the estate, there is a possibility that the applicant's actions will decrease the assets in the estate. For example, an applicant who resolves an ambiguity may discover that the value of the assets in the estate was less than initially projected. While the estate's value has been directly reduced, the applicant has nonetheless indirectly benefited the estate by resolving that issue before it could cause additional problems. The court should not bear the cost of resolving ambiguities when the debtor wants the true value to remain unknown. Instead, the estate should compensate the applicant for reasonable costs incurred when resolving this ambiguity.

Allowing reasonable compensation for indirect benefits should be restricted to when the applicant is acting in good faith. Applicants should not be rewarded for intentionally trying to lower the value of the estate out of their own self-interest. The good faith requirement here is imposed because applicants should be rewarded for trying to increase the value of the estate for the benefit of everyone involved in the bankruptcy proceedings. When that goal is being furthered, courts should not automatically bar the applicant from recovering some expenses through administrative priority solely because the benefit cannot be quantified.

Although rare, significant benefits to the estate that cannot be quantified should be encouraged. Applicants that confer benefits should not be excluded from administrative expense consideration because they did not directly add value to the estate. Instead, applicants should have the opportunity to seek reasonable compensation for their good faith efforts by showing that they indirectly benefited the estate.

*E. Neither the Text of 503(b)(3)(D) nor the Interpretations Provided by Common Law Require a Benefit to Be Quantifiable to Be a Substantial Contribution*

Congress drafted 11 U.S.C. § 503 without the term “quantifiable.”<sup>72</sup>

However, courts have interpreted the phrase “substantial contribution” in section 503(b)(3) inconsistently.<sup>73</sup> While this issue has been litigated and a wealth of opinions exist that shed light on a clear meaning, different interpretations are used by jurisdictions around the United States. While the requirement that a substantial contribution be quantifiable has been read into the text of § 503 (b)(3)(D), each core phrase described below has room to allow applicants to recover for indirect benefits as proposed by this Comment.

*1. The Core Phrases Used by Courts in Substantial Contribution Analysis Do Not Require that the Benefit to the Estate Be Quantifiable*

The definition of a substantial contribution is inconsistent,<sup>74</sup> “which consequently requires the courts to construe it in each individual case as a matter of judicial discretion, without the benefit of clear congressional guidance.”<sup>75</sup> Several “core phrases” are recited frequently in opinions dealing with substantial contributions. This language is used by courts to describe what a substantial contribution applicant must show. Unfortunately, the phrases often overlap, cause confusion, and prevent parties from participating in proceedings because of uncertainty. These core phrases include terms such as “foster,”<sup>76</sup> “enhance,”<sup>77</sup> “demonstrable,”<sup>78</sup> “indirect,”<sup>79</sup> “incidental,”<sup>80</sup> “minimal”<sup>81</sup> and “benefit.”<sup>82</sup> Despite their ubiquity, they offer little guidance to an applicant deciding whether to participate in bankruptcy proceedings.<sup>83</sup>

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<sup>72</sup> See generally 11 U.S.C. § 503 (2019).

<sup>73</sup> See Stone, *supra* note 23, at 227–28.

<sup>74</sup> See generally *In re R.L. Adkins Corp.*, 505 B.R. 770, 780–81 (Bankr. N.D. Tex. 2014) (quoting *In re Energy Partners, Ltd.*, 422 B.R. 68, 80 (Bankr. S.D. Tex. 2009) (citing *In re Mirant Corp.*, 354 B.R. 113 (Bankr. N.D. Tex. 2006)).

<sup>75</sup> Stone, *supra* note 23, at 226.

<sup>76</sup> *Pierson & Gaylen v. Creel & Atwood (In re Consolidated Bancshares, Inc.)*, 785 F.2d 1249, 1253 (5th Cir. 1986).

<sup>77</sup> *Id.*

<sup>78</sup> *In re Texaco, Inc.*, 90 B.R. 622, 630 (Bankr. S.D.N.Y. 1988).

<sup>79</sup> *In re Baldwin-United Corp.*, 79 B.R. 321, 341 (Bankr. S.D. Ohio 1987).

<sup>80</sup> See *In re 9085 E. Mineral Office Bldg., Ltd.*, 119 B.R. 246, 251 (Bankr. D. Colo. 1990).

<sup>81</sup> See *In re Baldwin-United Corp.*, 79 B.R. 321, 341 (Bankr. S.D. Ohio 1987).

<sup>82</sup> See *id.*

<sup>83</sup> Cohen, *supra* note 7, at 677 n.152.

Although this confusing language is the most commonly used standard for the substantial contribution analysis, some courts are already looking to expand the definition. One court stated that “[i]t would be inequitable and unfair to deny [the applicant] any compensation from the debtor’s estate” even though the Code provided no direct avenue for recovery.<sup>84</sup> The court also suggested that the language most often used by that jurisdiction, “Foster-and-Enhance-Rather-than-Retard-or-Interrupt-the-Reorganization-Process,” was just one possible basis for compensation under § 503.<sup>85</sup>

No matter the jurisdiction, room exists to allow for benefits to the estate that are not quantifiable to be given administrative expense priority. A selection of core phrases that are used commonly across the country is provided below.

*a. “Direct Benefit”*

The direct benefit rule is grounded in congressional language<sup>86</sup> and is the oldest and most ambiguous of the core phrases. It is a requirement that has been read into the text of § 503 that benefits to the estate must be direct to be considered a substantial contribution for administrative expense purposes. While it provides little guidance on its face, this rule has been developed into more specific language over the years. For example, one court considered (among other factors) “whether the applicant provided a ‘direct, significant, and demonstrably positive benefit’ to the estate. . . .”<sup>87</sup>

The phrase “substantial contribution” is “derived from §§ 242 and 243 of the former Bankruptcy Act.”<sup>88</sup> When utilizing or analyzing the direct benefit requirement, courts often cite the legislative history of the Bankruptcy Reform Act of 1978 that provides, “[the direct benefit rule] does not require a contribution that leads to confirmation of a plan, for in many cases, it will be a substantial contribution if the person involved uncovers facts that would lead to a denial of confirmation, such as fraud in connection with the case.”<sup>89</sup> This

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<sup>84</sup> *Id.* at 677 n.153 (citing *In re Glade Springs, Inc.*, 77 B.R. 184, 196 (Bankr. E.D. Tenn. 1987), *vacated*, 826 F.2d 440 (6th Cir. 1987)).

<sup>85</sup> *In re Glade Springs, Inc.*, 77 B.R. at 194, *vacated*, 826 F.2d 440 (6th Cir. 1987).

<sup>86</sup> H.R. REP. NO. 95-595, at 355 (1977).

<sup>87</sup> Stone, *supra* note 23, at 227 (quoting *In re Buckhead Am. Corp.*, 161 B.R. 11, 15 (Bankr. D. Del. 1993); *In re Alert Holdings, Inc.*, 157 B.R. 753, 757 (Bankr. S.D.N.Y. 1993) (citing *In re FRG, Inc.*, 124 B.R. 653, 658 (Bankr. E.D. Pa. 1991)); *In re Buttes Gas & Oil Co.*, 112 B.R. 191, 194 (Bankr. S.D. Tex. 1989)).

<sup>88</sup> *In re Jensen-Farley Pictures, Inc.*, 47 B.R. 557, 566 (Bankr. D. Utah 1985) (citing H.R. REP. NO. 95-595, at 355 (1977); *In re Grynberg*, 19 B.R. 621, 623 (Bankr. D. Colo. 1982) (“[Section] 503(b)(3)(D) is the progeny of § 243 . . .”).

<sup>89</sup> H.R. REP. NO. 95-595, at 186–87 (1977) (cited by *In re Grasso*, 519 B.R. 137, 142 (Bankr. E.D. Pa. 2014); *Lebron v. Mecham Fin. Inc.*, 27 F.3d 937, 945 (3d Cir. 1994)).



language is the oldest “test” used to understand the substantial contribution analysis and has been developed over the years into more precise rules and requirements.

*b. “Significance”*

Generally, the “Significance Test” is when a court “focuses upon the degree or significance of the contribution being considered.”<sup>90</sup> Under this test, applicants are required to show that they contributed “[s]omething more than minimal assistance to the estate. . . .”<sup>91</sup> Courts using this language require that the entities seeking reimbursement “prove that the expenses resulted in a significant and tangible benefit to the estate[.]”<sup>92</sup>

Some courts use the Significance Test as a “threshold measure to assess whether further inquiry is required.”<sup>93</sup> Jurisdictions using this approach require an applicant’s services to “reach a significant level” before proceeding further with the substantial contribution analysis.<sup>94</sup>

Other courts consider the significance of a benefit alongside the rest of the substantial contribution analysis.<sup>95</sup> This interpretation “parallels” the benefit to the estate test,<sup>96</sup> placing a focus on the benefit to the estate being “tangible.”<sup>97</sup>

The requirement that a benefit be “significant” is prevalent in the few opinions that delve into the relationship among the Code, the Trust Indenture Act and their legislative histories.<sup>98</sup> These opinions hold that this relationship requires the applicant to show an “actual direct and demonstrable benefit” to the estate.<sup>99</sup> This is a common core phrase used by many other opinions as well.<sup>100</sup>

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<sup>90</sup> *In re* 9085 E. Mineral Office Bldg., Ltd., 119 B.R. 246, 253 (Bankr. D. Colo. 1990).

<sup>91</sup> Cohen, *supra* note 7, at 677 (citing *In re* 9085 E. Mineral Office Bldg., Ltd., 119 Bankr. 246, 253 (Bankr. D. Colo. 1990); *see also In re D’Lites of Am., Inc.*, 108 Bankr. 352, 356 (Bankr. N.D. Ga. 1989) (applicant must prove both significant and tangible benefits).

<sup>92</sup> *In re D’Lites of Am., Inc.*, 108 B.R. at 356.

<sup>93</sup> Cohen, *supra* note 7, at 677.

<sup>94</sup> *Id.* (citing *In re* 9085 E. Mineral Office Bldg., Ltd., 119 B.R. at 253); *see also In re D’Lites of Am., Inc.*, 108 B.R. at 356 (applicant must prove both significant and tangible benefits).

<sup>95</sup> *In re* 9085 E. Mineral Office Bldg., Ltd., 119 B.R. at 253; *see also In re D’Lites of Am., Inc.*, 108 B.R. at 356 (the applicant was required to prove that the benefit was both significant and tangible).

<sup>96</sup> Cohen, *supra* note 7, at 666.

<sup>97</sup> *In re D’Lites of Am., Inc.*, 108 B.R. at 356.

<sup>98</sup> *See* Caplin v. Marine Midland Grace Tr. Co. of New York, 406 U.S. 416, 422; *In re* Pacific Homes, 20 B.R. 729, 749–50 (Bankr. C.D. Cal. 1982); *In re* Yale Express Sys., Inc., 366 F.Supp. 1376, 1387–88 (S.D.N.Y. 1973).

<sup>99</sup> Mark A. Cohen, Reimbursement of Indenture Trustees for Substantial Contribution Under Section 503 of the Bankruptcy Code, 59 FORDHAM L. REV. 647, 667 (1991).

<sup>100</sup> *See, e.g., In re* R.L. Adkins Corp., 505 B.R. 770, 780–81 (Bankr. N.D. Tex. 2014); *In re* Energy

The strict language of the Significance Test requires the benefit to be conferred on “the debtor’s estate, the creditors, and to the extent relevant, the stockholders.”<sup>101</sup> Similar language was used by one district court in the First Circuit that required “a measurable and valuable benefit to the Debtor’s estate.”<sup>102</sup>

Some courts require that those looking for reimbursement of administrative assets “demonstrate that their services were exceptional.”<sup>103</sup> However, it does not follow that services that cannot be quantified can never provide an actual and demonstrable benefit or be exceptional enough to receive an allowance.

*i. Case Analysis*

Further analysis of this test is required because there is a specific split in authority that is worth highlighting. The Bankruptcy Court for the Northern District of Georgia distinguished facts that satisfied the significance test from those that would not in *In re D’Lites of America, Inc.*<sup>104</sup> In *In re D’Lites*, the applicant, Walton Investments, Inc., began running the debtor’s business using Walton employees in an attempt to keep it operational and ultimately worth more.<sup>105</sup> The court compared the facts there with those of a case heard by the Seventh Circuit Court of Appeals in *Park Terrace*.<sup>106</sup> In *Park Terrace*, the applicant “instituted a marketing program which significantly increased occupancy rates and monthly income” at the debtor’s property.<sup>107</sup>

From the facts presented so far, both applicants took actions intending to make the estate more valuable. Before looking at how the court reached its conclusion in *In re D’Lites of Am., Inc.*, it is important to establish that Walton Investments made two loans of \$250,000 and replaced D’Lites employees for the purpose of purchasing the company.<sup>108</sup> There is a split of authority on the issue of considering a creditor’s motives when conducting a substantial

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Partners, Ltd., 422 B.R. 68, 80 (Bankr. S.D. Tex. 2009); *In re Mirant Corp.*, 354 B.R. 113, 132–35 (Bankr. N.D. Tex. 2006).

<sup>101</sup> *In re Granite Partners*, 213 B.R. 440, 445 (Bankr. S.D.N.Y. 1997); Stone, *supra* note 23, at 252 (citing Haskins v. United States (*In re Lister*), 846 F.2d 55, 57 (10th Cir. 1988).

<sup>102</sup> *In re Boston and Me. Corp.*, 62 B.R. 199, 203 (D. Mass. 1986).

<sup>103</sup> Matter of W.T. Grant Co., 85 B.R. 250, 264 (Bankr. S.D.N.Y. 1988), *aff’d* in part, *rev’d* in part sub nom. *In re W.T. Grant Co.*, 119 B.R. 898 (S.D.N.Y. 1990), *aff’d* sub nom. *In re W.T. Grant Co.* 935 F.2d 1277 (2d Cir. 1991).

<sup>104</sup> *In re D’Lites of Am., Inc.*, 108 B.R. 352, 356 (Bankr. N.D. Ga. 1989).

<sup>105</sup> *Id.* at 354 (citing *Park Terrace Townhouses v. Wilds*, 852 F.2d 1019 (7th Cir. 1988)).

<sup>106</sup> *Park Terrace Townhouses*, 852 F.2d 1019.

<sup>107</sup> *In re D’Lites of Am., Inc.*, 108 B.R. at 356 (citing *Park Terrace Townhouses*, 852 F.2d 1019).

<sup>108</sup> *Id.* at 354.

contribution analysis.<sup>109</sup> The vast majority of jurisdictions “deny reimbursement where the applicant’s actions are self-interested and duplicative.”<sup>110</sup> An applicant acting in their own interest is sufficient evidence to deny the claim here because this court adheres to the ruling that an applicant is not entitled to administrative expense priority when acting in its own interest rather than the interest of the estate.<sup>111</sup>

Two key distinctions were made by the court in *In re D’Lites of Am., Inc.*, with the first providing a good illustration of the current understanding of a “significant” benefit to the estate. This opinion will be used to illustrate how the interpretation of the substantial contribution proposed by this Comment is consistent with current precedent. Also, remember, this analysis was used by the court to demonstrate that Walton Investments, Inc. was acting out of personal interest, not that these issues would preclude administrative expense priority otherwise.

The applicant in *Park Terrace* was awarded administrative expenses because he “provided a significant and tangible benefit to the estate by maintaining, upgrading and remodeling the debtor’s rental units, and by increasing occupancy rates and monthly income[.]”<sup>112</sup> The applicant in *In re D’Lites of Am., Inc.*, however, “sustained approximately \$700,000.00 in losses during its operating effort [to keep the business afloat.]”<sup>113</sup> The applicant “insist[ed] that the continued operation of the business increased the value of [the debtor’s] assets at the time of sale,” but the court was unwilling to award administrative expenses because the applicant did not “quantify the benefit to the estate.”<sup>114</sup>

This comparison provides an opportunity to illustrate how this Comment proposes to change the interpretation of the substantial contribution analysis. The applicant in *Park Terrace* made a substantial contribution to the estate under the current understanding because he increased occupancy rates and monthly income.<sup>115</sup> The applicant in *In re D’Lites* did not make a substantial contribution under the current understanding because the business lost money due to its

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<sup>109</sup> *In re* 1250 Oceanside Partners, 519 B.R. 802, 807 (Bankr. D. Haw. 2014) (citing *In re Cellular 101, Inc.*, 377 F.3d 1092, 1097 (9th Cir. 2004)).

<sup>110</sup> Cohen, *supra* note 7, at 647, 672–73 n.163.

<sup>111</sup> *In re D’Lites of Am., Inc.*, 108 B.R. at 357 (citing *In re Lister*, 846 F.2d 55, 57 (10th Cir. 1988); *In re Patch Graphics*, 58 B.R. 743, 746 (Bankr. W.D. Wis. 1986); *In re McK, Ltd.*, 14 B.R. 518, 520 (Bankr. D. Colo. 1981)) (“When a creditor incurs expenses primarily to protect its own interests rather than the interests of the estate, the creditor is not entitled to a priority claim.”).

<sup>112</sup> *In re D’Lites of Am., Inc.*, 108 B.R. at 356 (citing *Park Terrace Townhouses* 852 F.2d 1019).

<sup>113</sup> *Id.*

<sup>114</sup> *Id.*

<sup>115</sup> *See Park Terrace Townhouses*, 852 F.2d 1019.

efforts. However, both applicants provided benefits to the estate that cannot be quantified.

The *Park Terrace* applicant maintained, upgraded and remodeled the debtor's rental units which led to the significant benefit to the estate.<sup>116</sup> The *In re D'Lites* applicant provided \$500,000 in loans and staffed the failing business with new employees.<sup>117</sup> These applicants both contributed unquantifiable benefits to the estate that should be considered when awarding administrative expenses.<sup>118</sup> If the *Park Terrace* townhomes lost money after the applicant renovated them due to unrelated circumstances, he would not be able to point to a "quantifiable" benefit to secure administrative expense priority.<sup>119</sup> Similarly, D'Lites lost money under Walton Investments despite its efforts to turn the business around.<sup>120</sup> The substantial contribution analysis should include actions taken by the applicant that positively impact the debtor's estate, including but not limited to generating additional assets. Allowing applicants to recover reasonable expenses (as opposed to actual expenses) for clear indirect benefits will reduce the chilling effect on participation and encourage meaningful participation for all. Even if an applicant loses money because of their efforts, allowing reasonable expenses for their good faith effort prevents a total loss.

c. "*Tangible Benefit*"

This language, along with the "actual-direct-and-demonstrable-benefit test," have manifested as more precise evolutions of the traditional "benefit-to-the-estate test."<sup>121</sup> Both tests appear to be grounded in the Chandler Act,<sup>122</sup> which amended the bankruptcy code in the United States as it existed in 1938.<sup>123</sup> Sections 64a(1), 242 and 243 of the Chandler Act served as the basis for § 503(b) of the 1978 Code.<sup>124</sup> As both tests are rooted in the original language that formed § 503 of the modern Code, their "differences are based almost exclusively on the terms that courts select to define the type of benefit necessary to satisfy the substantial contribution standard."<sup>125</sup> Following the common theme in this area

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<sup>116</sup> *See id.*

<sup>117</sup> *In re D'Lites of Am., Inc.*, 108 B.R. at 356.

<sup>118</sup> *See id.*; *Park Terrace Townhouses*, 852 F.2d 1019.

<sup>119</sup> *See generally Park Terrace Townhouses*, 852 F.2d 1019.

<sup>120</sup> *In re D'Lites of Am., Inc.*, 108 B.R. 352, 356 (Bankr. N.D. Ga. 1989).

<sup>121</sup> Cohen, *supra* note 7, at 650.

<sup>122</sup> *Id.*

<sup>123</sup> *Id.* at 655.

<sup>124</sup> *See* H.R. REP. NO. 95-595, at 355 (1977).

<sup>125</sup> Cohen, *supra* note 7, at 677 n.20.

of the law, what separates the practical use of these tests is merely conflicting judicial interpretation.

The phrase *tangible benefit*,<sup>126</sup> like *actual and demonstrable benefit*, requires a material benefit to be made to the estate.<sup>127</sup> A requirement that a benefit be material should not mandate that it be quantifiable. The tangible benefit requirement is currently interpreted to mandate quantifiable benefits before a substantial contribution is found,<sup>128</sup> but this should be changed. There is no statutory language that ties “tangible” with “quantifiable.” While some precedent compares the two terms, they can easily be distinguished.<sup>129</sup>

This Comment argues that a benefit can be material without being quantifiable in many circumstances. Reducing costs to the estate is a material benefit but is not quantifiable under the current interpretation in many jurisdictions. Improving the marketing outreach and consumer perception of a brand can provide a major material benefit to a debtor, but putting a number on these figures requires expensive guesswork. Rather than requiring a quantifiable benefit, courts should instead allow for applicants to demonstrate how they have benefited the estate and allow for reasonable compensation for their efforts.

Unlike the language described above, the following tests are not rooted in legislative language or intent but judicial creations.<sup>130</sup> Both tests “look to the overall effect on the reorganization process due to the claimant’s actions” rather than adhering to the language provided by Congress.<sup>131</sup>

*d. The Preference That the Benefit “Foster-And-Enhance-Rather-Than-Retard-Or-Interrupt-The-Reorganization-Process”*

The vague language of this phrase allows courts to interpret the substantial contribution analysis as needed on a case-by-case basis. Relying on this language grants courts the freedom to “employ notions of equity, fairness[,] and judicial independence to interpret the text of [§] 503 and develop standards to judge or justify questionable or controversial fee and expense awards or to

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<sup>126</sup> Stone, *supra* note 23, at 252 (citing *In re Envirodyne Indus., Inc.*, 176 B.R. 815, 819 (Bankr. N.D. Ill. 1995); *In re Jack Winter Apparel, Inc.*, 119 B.R. 629, 633 (Bankr. E.D. Wis. 1990)).

<sup>127</sup> See Cohen, *supra* note 7, at 670.

<sup>128</sup> *In re New Power Co.*, 311 B.R. 118, 126 (Bankr. N.D. Ga. 2004).

<sup>129</sup> *In re W.T. Grant Co.*, 119 B.R. 898 (S.D.N.Y. 1990) (“The Second Circuit has recognized the “lodestar” principle whereby a basic per hour rate is multiplied by a factor which takes into account both results achieved and quality of services rendered.”).

<sup>130</sup> See Cohen, *supra* note 7, at 650 (“The foster-and-enhance-rather-than-retard-or-interrupt-the-progress-of-reorganization test and the but-for test seem to be judicial creations less rooted in legislative action.”).

<sup>131</sup> *Id.* at 650 n.21.

support a claim of fostering and enhancing the process of reorganization.”<sup>132</sup> This vagueness “signifies a judicial reaction to the lack of congressional guidance in the statutory language of [§] 503.”<sup>133</sup>

A more liberal approach to the role of judicial discretion gives courts the ability to bend this test to allow applicants to recover benefits that do not fit exactly within the confines of § 503.<sup>134</sup> A more conservative view, however, limits the court’s discretion to the “well-established construction of the statute.”<sup>135</sup> It would be easiest to make the proposed change of the language in § 503 to the liberal view, as it allows for the broadest level of discretion.

#### *i. Case Analysis*

This “foster and enhance” language was used by the Fifth Circuit Court of Appeals in the frequently cited case, *In re Consolidated Bancshares, Inc.*<sup>136</sup> There, the Court cites to commonly used language that administrative expense priority should be granted because “services which substantially contribute to a case are those which foster and enhance, rather than retard or interrupt the progress or reorganization.”<sup>137</sup> The Court goes on to discuss when compensation is denied, citing to the Bankruptcy Court in the Eastern District of New York: “Compensation has been denied where the services rendered by the creditor or shareholder were only ‘remotely related to the reorganization[.]’”<sup>138</sup> The reasoning behind this is that, “a creditor’s attorney must ordinarily look to its own client for payment, unless the creditor’s attorney rendered services on behalf of the reorganization, not merely on behalf of his client’s interest, and conferred a significant and demonstrable benefit to the debtor’s estate and the creditors.”<sup>139</sup> Whether services relate to the reorganization independent of selfish interests is a fine indicator for whether administrative expense priority should be granted. Additionally, this indicator has nothing to do with whether the services are quantifiable.

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<sup>132</sup> *Id.* at 671 (citing to *In re K-FAB, Inc.*, 118 Bankr. 240, 242 (M.D. Pa. 1990) (“[F]ee determination . . . must be a consideration of the overall ‘fairness and reasonableness’” of the fee under all of the circumstances).

<sup>133</sup> *Id.*

<sup>134</sup> *Id.*

<sup>135</sup> *Id.* (citing *Grundy Nat’l Bank v. Rife (In re Rife)*, 71 Bankr. 129, 131 (Bankr. W.D. Va.)).

<sup>136</sup> *In re Consol. Bancshares, Inc.*, 785 F.2d 1249, 1253 (5th Cir. 1986) (quoting *In re White Motor Credit Corp.*, 50 B.R. 885, 892 (Bankr. N.D. Ohio 1985) (internal quotations omitted)).

<sup>137</sup> *Id.*

<sup>138</sup> *In re Consol. Bancshares, Inc.*, 785 F.2d at 1253 (citing *In re Gen. Oil Distrib., Inc.*, 51 B.R. 794, 806 (Bankr. E.D.N.Y. 1985)).

<sup>139</sup> *In re Gen. Oil Distrib., Inc.*, 51 B.R. at 806 (emphasis removed).

Like the analysis of the *In re D'Lites* and *Park Terrace* cases above, *In re Consolidated Bancshares, Inc.* provides an opportunity to demonstrate how the solution proposed by this Comment would be incorporated into a real set of facts.<sup>140</sup> As illustrated above, there are several issues with the applicant's request that serve as the basis for denial of the request.

First, the applicants were a group of attorneys seeking compensation for services that were also completed by the court-appointed equity security holders' committee.<sup>141</sup> These services, performed after the appointment of the equity security holders committee, were therefore duplicative in time and effort, a fact that was fatal to their request for administrative expense priority.<sup>142</sup>

Second, the applicants were motivated by a personal interest, not for the benefit of the chapter 11 estate.<sup>143</sup> As discussed above, a showing that the applicant was primarily motivated by personal interest rather than the benefit of the estate is fatal to administrative expense priority.<sup>144</sup>

Third, the action that the applicants performed was meritless.<sup>145</sup> As the state lawsuit became property of the estate once the bankruptcy petition was filed, "the lawsuit could have been dismissed for lack of a proper party plaintiff, i.e., the debtor, and therefore had little value to the bankruptcy estate."<sup>146</sup>

This Comment does not propose to eliminate the issues in this case listed above from serving as sufficient evidence to deny administrative expense priority. Instead, focus on the fact that the court had three distinct rationales to decide the case on and still chose to cite "Foster-and-Enhance-Rather-than-Retard-or-Interrupt-the-Reorganization-Process" language.<sup>147</sup> Including this language serves no purpose in this decision and should be viewed as dicta. Instead, this has been cited numerous times for that exact language in other administrative expense cases.<sup>148</sup>

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<sup>140</sup> *In re Consol. Bancshares, Inc.*, 785 F.2d at 1253.

<sup>141</sup> *Id.* at 1252.

<sup>142</sup> See *In re R.L. Adkins Corp.*, 505 B.R. 770, 780–81 (Bankr. N.D. Tex. 2014); *In re Energy Partners, Ltd.*, 422 B.R. 68, 80 (Bankr. S.D. Tex. 2009); *In re Mirant Corp.*, 354 B.R. 113, 132–35 (Bankr. N.D. Tex. 2006).

<sup>143</sup> *In re Consol. Bancshares, Inc.*, 785 F.2d at 1252.

<sup>144</sup> See generally *In re Lister*, 846 F.2d 55, 57 (10th Cir. 1988); *In re Patch Graphics*, 58 B.R. 743, 746 (Bankr. W.D. Wis. 1986) ("When a creditor incurs expenses primarily to protect its own interests [rather than the interests of the estate,] the creditor is not entitled to a priority . . . claim.").

<sup>145</sup> *In re Consol. Bancshares, Inc.*, 785 F.2d at 1252.

<sup>146</sup> *Id.*

<sup>147</sup> *Id.*

<sup>148</sup> See generally *Lebron v. Mechem Fin. Inc.*, 27 F.3d 937, 944 (3d Cir. 1994); *Batiste v. Sun Kona Fin. I, LLC*, No. CV 15-00397 ACK-KSC, 2017 U.S. Dist. LEXIS 4936 at \*5 (D. Haw. Jan. 12, 2017).

This language was cited by the Ninth Circuit Court of Appeals in *In re Cellular 101, Inc.*<sup>149</sup> There, the Court cited this language when determining if a bankruptcy court had made an error by granting administrative expense priority to an applicant that proposed the only reorganization plan that was put before it.<sup>150</sup> Assisting the successful implementation of a reorganization plan was specifically laid out by Congress as a substantial contribution to the estate.<sup>151</sup> As the only plan submitted to the bankruptcy court was proposed by the applicants, they were clearly instrumental in its success.

This test does not clarify the substantial contribution analysis for courts, applicants, or debtors. It appears to be a statement devoid of meaning that is added to justify whatever analysis a court has decided to conduct. For jurisdictions using this language, judges have total freedom to interpret it as allowing administrative expense priority to applicants that have made a substantial contribution without being able to quantify it. The broad language of this test should be used to allow for administrative expenses for applicants who fostered and enhanced the reorganization process, regardless of whether their contribution can be quantified.

*e. “But-For”*

This language is based in tort law and is rarely used by courts in an administrative expense context. Regardless, some courts require a showing that, but for the actions of the applicant, the efforts of the case would be substantially diminished.<sup>152</sup>

This test demonstrates how widely the approaches of courts have varied and “illustrates the lack of unity in the standards and creates a possibility of unjust results because of the emphasis on different factors.”<sup>153</sup> Regardless, a but-for standard, if used by a court, should allow administrative expenses for applicants who benefited the estate, even if that benefit cannot be quantified.

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<sup>149</sup> *In re Cellular 101, Inc.*, 377 F.3d 1092, 1096 (9th Cir. 2004) (citing *In re Consolidated Bancshares, Inc.*, 785 F.2d 1249, 1253 (5th Cir. 1986)).

<sup>150</sup> *Id.*

<sup>151</sup> See S. REP. NO. 95-598, at 66–67 (1978) (“The phrase ‘substantial contribution in a case’ . . . does not require a contribution that leads to confirmation of a plan, for in many cases, it will be a substantial contribution if the person involved uncovers facts that would lead to a denial of confirmation . . .”).

<sup>152</sup> Cohen, *supra* note 7, at 677 (internal quotations omitted).

<sup>153</sup> Cohen, *supra* note 7, at 672.



The Fifth Circuit uses a cost-benefit analysis developed from a wide range of opinions dealing with substantial contributions.<sup>154</sup> This analyzes substantial contributions on a case by case basis and requires that courts “weigh the cost of the claimed fees and expenses against the benefits conferred upon the estate which flow directly from those actions.”<sup>155</sup> Those benefits that are only conferred upon a portion of the estate are diminished in weight by the analysis and are less likely to receive expenses.<sup>156</sup>

*F. The Phrase “Actual and Necessary” in Section 503(B)(3) Does Not Require That the Benefit to the Estate Be Quantifiable*

The analysis above focused on the requirement that an applicant substantially contribute to the estate but there are other requirements that must be met as well. While this Comment focuses primarily on § 503(b)(3)(D), all requirements of § 503(b)(3) must be met before subsection (D) is considered.

Section 503(b)(3) of the Code requires that applicants prove their benefit to the estate was actual and necessary.<sup>157</sup> The language used by courts when making this determination is discussed below.

*1. The Four Main Ideas by Courts in “Actual and Necessary” Analysis Do Not Require That the Benefit to the Estate Be Quantifiable*

Each of the following factors preclude an applicant from receiving administrative expense priority because they are fatal to a claim that the contribution was actual and necessary.

First, the court weighs the cost of administrative expense repayment against the benefit conferred by the applicant.<sup>158</sup> A substantial contribution is more likely to be found if the benefit conferred by the applicant exceeds the cost that the applicant seeks to assess against the estate.<sup>159</sup>

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<sup>154</sup> See, e.g., *In re Am. Plumbing & Mech., Inc.*, 327 B.R. 273, 281 (Bankr. W.D. Tex. 2005).

<sup>155</sup> *In re DP Partners Ltd. P’ship*, 106 F.3d 667, 673 (5th Cir. 1997).

<sup>156</sup> *Id.*

<sup>157</sup> 11 U.S.C. § 503(b)(3) (2019).

<sup>158</sup> See *In re R.L. Adkins Corp.*, 505 B.R. 770, 780–81 (Bankr. N.D. Tex. 2014); *In re Energy Partners, Ltd.*, 422 B.R. 68, 80 (Bankr. S.D. Tex. 2009); *In re Mirant Corp.*, 354 B.R. 113, 132–35 (Bankr. N.D. Tex. 2006).

<sup>159</sup> See *In re R.L. Adkins Corp.*, 505 B.R. at 780–81; *In re Energy Partners, Ltd.*, 422 B.R. at 80; *In re Mirant Corp.*, 354 B.R. at 132–35.

Second, the benefit is scrutinized to ensure it was not the result of duplicative efforts, which would allow multiple applicants to get paid for the same result.<sup>160</sup> Courts are reluctant to find that a contribution was necessary when the applicant's efforts were duplicative of efforts undertaken by statutory fiduciaries.<sup>161</sup> This requires judges to "scrutinize claimed expenses for waste and duplication[,]"<sup>162</sup> but allows freedom to make this determination however they see fit.<sup>163</sup>

Third, it is usually fatal for a substantial contribution claim if the applicant is found to have negatively impacted the estate through their efforts.<sup>164</sup> A finding that the applicant had a negative effect on the case is often fatal to an administrative expense claim.<sup>165</sup> This is a broad category and can include detrimental actions such as making questionable objections to pleadings filed by the debtor or engaging in some other improper conduct that caused the debtor to incur costs or that delayed resolution of a case.

Fourth, administrative expenses are usually denied if the applicant's participation was primarily motivated to benefit themselves rather than the estate.<sup>166</sup> However, "[m]ost activities of an interested party that contribute to the estate will also, of course, benefit that party to some degree, and the existence of a self-interest cannot in and of itself preclude reimbursement."<sup>167</sup>

Regardless of the applicant's ability to quantify a benefit, administrative expenses should not be granted if the applicant's contributions have a negative impact on the estate. While applicants can take a risk that may or may not work out in favor of the estate, there must be an agreement between the parties before this takes place. Allowing administrative expenses for an applicant that unilaterally decides to gamble in the proceedings regardless of the outcome goes

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<sup>160</sup> See *In re R.L. Adkins Corp.*, 505 B.R. at 780–81; *In re Energy Partners, Ltd.*, 422 B.R. at 80; *In re Mirant Corp.*, 354 B.R. at 132–35.

<sup>161</sup> See *In re R.L. Adkins Corp.*, 505 B.R. at 780–81; *In re Energy Partners, Ltd.*, 422 B.R. at 80; *In re Mirant Corp.*, 354 B.R. at 132–35.

<sup>162</sup> *In re DP Partners Ltd. P'ship*, 106 F.3d 667, 673 (5th Cir. 1997).

<sup>163</sup> *Id.* (citing *In re Lister*, 846 F.2d 55, 57 (10th Cir. 1988)).

<sup>164</sup> See *In re R.L. Adkins Corp.*, 505 B.R. at 780–81.

<sup>165</sup> See *id.*

<sup>166</sup> *In re Kior, Inc.*, 567 B.R. 451, 459 (D. Del. 2017) (citing *Lebron v. Mechem Fin. Inc.*, 27 F.3d 937, 944 (3d Cir. 1994)).

<sup>167</sup> *Lebron v. Mechem Fin.*, 27 F.3d 937, 944 (3d Cir. 1994).

against the purpose of § 503<sup>168</sup> and will inevitably lead to “mushrooming” expenses.<sup>169</sup>

This Comment does not propose to alter the requirement that a benefit be actual and necessary to the estate. Instead, this analysis should be left alone and treated as separate from the substantial contribution analysis discussed above. When courts describe the analysis of the actual and necessary requirement alongside the substantial contribution analysis, language from both can be conflated. As discussed in the substantial contribution breakdown above, this leads to confusion of courts, applicants, and debtors alike.

### *G. Benefits of the Solution Proposed by this Comment*

The solution proposed by this Comment will further the competing goals of bankruptcy and increase judicial efficiency without significant change or effort. Both benefits are discussed below.

#### *1. This Solution Furthers the Competing Goals of Bankruptcy*

Section 503 of the Code is understood to apply to a narrow set of circumstances because it must balance promoting meaningful participation with keeping costs to the estate to a minimum.<sup>170</sup> Both goals will be met if substantial contributions include benefits to the estate that do not quantifiably increase its assets. It is established that substantial contribution awards are uncommon, as they are “reserved for those rare and extraordinary circumstances when the creditor’s involvement truly enhances the administration of the estate.”<sup>171</sup>

The rarity of these expenses is indicative of how hard it is for an applicant to show that they substantially contributed to a case. More applicants who meet both goals of § 503 should be reimbursed for their efforts because everyone benefits as a result. This would further the goal of § 503(b)(3)(D) “to encourage activities that will benefit the estate as a whole[.]”<sup>172</sup> When applicants benefit the estate more than their expenses will cost, there is a net gain for the debtor. Even if the value of the payment to the applicant is adjusted to account for the

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<sup>168</sup> See H.R. REP. NO. 95-595, at 355 (1977) (“Those who must wind up the affairs of a debtor’s estate must be assured of payment, or else they will not participate in the liquidation or distribution of the estate.”) (emphasis in original).

<sup>169</sup> *In re Am. Plumbing & Mech., Inc.*, 327 B.R. 273, 279 (Bankr. W.D. Tex. 2005).

<sup>170</sup> *In re Kior, Inc.*, 567 B.R. at 459.

<sup>171</sup> *Id.* (citing *In re RS Legacy Corp.*, No. 15-10197, 2016 Bankr. LEXIS 854, at \*1, \*3 (Bankr. D. Del. Mar. 17, 2016).

<sup>172</sup> Stone, *supra* note 23, at 234 (quoting *Lebron v. Mechem Fin., Inc.*, 27 F.3d 937, 944 (3d Cir. 1994)).

premium on liquid assets for a debtor, applicant contributions can outweigh administrative expense costs.<sup>173</sup> Failure to compensate applicants for their efforts goes against the goals of § 503(b)(3)(D) and reduces the efficiency of bankruptcy proceedings.<sup>174</sup>

*a. Judicial Efficiency*

Encouraging applicants to meaningfully participate in proceedings, especially in circumstances where their participation will provide a benefit to the estate, will create a more cooperative bankruptcy process and allow bankruptcy judges to spend more time on the more complicated matters in a case. Judges should be willing to allow the most qualified parties to participate in proceedings, regardless of the party. If a creditor is the best candidate to wrangle the various parties who will be voting on the reorganization plan, that creditor should be allowed to do so with the assurance that reasonable costs will be paid for its efforts.

*b. By Addressing Problems Earlier in a Case, Applicants Save Precious Time and Money*

Congress intended for § 503 to promote meaningful creditor participation while keeping costs of the estate to a minimum.<sup>175</sup> This goal is only satisfied if applicants—and the attorneys representing them—are provided with meaningful incentives. Administrative expenses provide a significant benefit, but are rarely granted.<sup>176</sup> The risk that these expenses will not be recovered makes participating in bankruptcy proceedings a difficult choice to make.<sup>177</sup> A court refusing to grant administrative expenses when a significant contribution is made unjustly enriches the debtor.<sup>178</sup>

In situations where an applicant makes a substantial contribution to the estate, an analogy can be drawn to a medical emergency.<sup>179</sup> When a medical professional assists an injured party in an emergency, there are two justifications

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<sup>173</sup> *In re R.L. Adkins Corp.*, 505 B.R. 770, 782–84 (Bankr. N.D. Tex. 2014).

<sup>174</sup> H.R. REP. NO. 95-595, at 186–87 (1977); *see generally In re U.S. Lines, Inc.*, 103 B.R. 427, 429 (Bankr. S.D.N.Y. 1989), *aff'd*, 1991 U.S. Dist. LEXIS 5262 (S.D.N.Y. Apr. 22, 1991).

<sup>175</sup> H.R. REP. NO. 95-595, at 186–87 (1977).

<sup>176</sup> Stone, *supra* note 23, at 223.

<sup>177</sup> *Id.* at 248 (citing RESTATEMENT (FIRST) OF RESTITUTION AND UNJUST ENRICHMENT § 116 (AM LAW INST., Proposed Final Draft, 1936)).

<sup>178</sup> *Id.* (citing RESTATEMENT (FIRST) OF RESTITUTION AND UNJUST ENRICHMENT § 116 (AM. LAW INST., Proposed Final Draft, 1936)).

<sup>179</sup> *Id.* (citing RESTATEMENT (FIRST) OF RESTITUTION § 116 (AM. LAW INST., Proposed Final Draft, 1936)).

for why the party should compensate the professional for their services. First, the injured party would—if able—undoubtedly agree to pay for the procedure.<sup>180</sup> The second is that, in an emergency, delaying treatment would be harmful to the party.<sup>181</sup>

A similar situation occurs when an applicant for administrative expenses confers a substantial contribution on the estate by exposing a problem that would cost the estate.<sup>182</sup> When a problem is solved before it arises, it is difficult to determine how much of a benefit the applicant conferred upon the estate. Although no assets were put into the estate, the cost of addressing the problem after it arose gets offset, benefitting the bottom line.

The debtor would almost certainly rather pay the applicant for its efforts than allow the reorganization to fail. While some issues may be fixable but expensive, others would cause the case to be dismissed or transferred to chapter 7. Additionally, as bankruptcy cases move quickly, waiting for court approval before acting may result in significant costs to creditors and the estate.

#### *H. Alternative Solutions*

Though bankruptcy courts have the discretion necessary to implement this change through their broad § 105 authority,<sup>183</sup> other solutions may achieve the same result. Finding new ways to quantify benefits previously precluded because they were nonquantifiable is one such solution. Implementing the common fund doctrine is another alternative that would achieve the results suggested by this Comment. Courts may also alter their definition of what constitutes a tangible benefit and make these changes on a case-by-case basis. Allowing applicants themselves to make this argument is a similar solution that places the burden on litigants rather than the judiciary. Judicial interpretation can be altered in several ways, including § 105<sup>184</sup> discretion. Finally, a direct change to § 503 by Congress would be the most direct way to implement the change proposed by this Comment.

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<sup>180</sup> *Id.* at 248–49 (citing RESTATEMENT (FIRST) OF RESTITUTION § 116 (AM. LAW INST., Proposed Final Draft, 1936)).

<sup>181</sup> *Id.* at 249 (citing RESTATEMENT (FIRST) OF RESTITUTION § 116 (AM. LAW INST., Proposed Final Draft, 1936)).

<sup>182</sup> *Id.* (citing RESTATEMENT (FIRST) OF RESTITUTION § 116 (AM. LAW INST., Proposed Final Draft, 1936)).

<sup>183</sup> See 11 U.S.C. § 105 (2019).

<sup>184</sup> See 11 U.S.C. § 105(a) (2019).

### 1. *Implementing New Methods of Quantifying Benefits*

While courts can easily alter what constitutes a quantifiable benefit, the same result will occur when implementing new methods of quantification.

#### a. *A Cost-Benefit Analysis Can Be Used to Quantify Some Benefits, Especially Those That Save the Estate Money Rather Than Increasing Its Assets*

A cost-benefit analysis that considers nonquantifiable contributions to the estate will allow all applicants who assist the estate to be rewarded for their efforts while preventing unnecessary costs to the estate. Increasing the assets of the bankruptcy estate is a well-established way to receive administrative expenses. If an applicant can show their efforts saved substantially more assets of the estate than their expenses suggest, they should be entitled to administrative expenses.<sup>185</sup> After all, “[a] penny saved is a penny earned.”<sup>186</sup>

A good faith component would also discourage poor behavior by applicants. The *In re Adelpia Communications Corp.* court rewarded negative conduct when it granted a bondholder group administrative expenses for making motions that, if granted, would have been disastrous for creditor recovery.<sup>187</sup> Their efforts caused other groups to invest in the proceedings, leading to increased assets for the bankruptcy estate.<sup>188</sup> Although this contribution would meet the proposed cost-benefit analysis, this kind of behavior should not be encouraged by bankruptcy courts.

The Fifth<sup>189</sup> and Ninth<sup>190</sup> Circuit already use a cost-benefit analysis to determine whether a substantial contribution has been made. Allowing applicants to demonstrate that their efforts benefited the estate more than the expenses they seek would not add a great deal to the judicial workload and would greatly increase efficiency.

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<sup>185</sup> See *In re Living Hope Se., LLC*, 509 B.R. 649 (Bankr. E.D. Ark. 2014) where a bankruptcy trustee in a chapter 7 case was entitled to administrative expense priority in a subsequent chapter 11 case because he made a substantial contribution to preserve assets that belonged to the debtor’s bankruptcy estate when he persuaded the court to appoint a chapter 11 trustee.

<sup>186</sup> E. Nesbit, *The Robber and the Burglar*, PALL MALL MAG. 107 (1899).

<sup>187</sup> *In re Adelpia Commc’ns Corp.*, 368 B.R. 140, 159 (Bankr. S.D.N.Y. 2007).

<sup>188</sup> *Id.* at 160.

<sup>189</sup> *In re Consolidated Bancshares, Inc.*, 785 F.2d 1249, 1252 (5th Cir. 1986).

<sup>190</sup> *In re Cellular 101, Inc.*, 377 F.3d 1092, 1096–97 (9th Cir. 2004).

b. *The Common Fund Doctrine Can Be Used as an Alternative Method and Rationale for Granting Recovery to Applicants*

A solution similar to the cost-benefit analysis was discussed in *Encouraging Creditor Participation: Integrating the Allowance of Administrative Expenses with the Common Fund Theory*.<sup>191</sup> The Supreme Court created the common fund doctrine in *Trustees of the Internal Improvement Fund v. Greenough*.<sup>192</sup> There, attorneys who brought in additional funds for a class were allowed payment from those assets.<sup>193</sup> The Court reasoned that a trustee in this scenario would have been granted expenses from the increased funds and that the attorney had provided the same benefit.<sup>194</sup>

Implementing the common fund doctrine to the administrative expense analysis would allow for any quantifiable increase in assets to be used to pay applicants, but it can also be applied to nonquantifiable benefits. Once an applicant has shown a substantial contribution to the estate, the applicant will then need to prove that the benefit the estate received is greater than the expenses it seeks. If these requirements are met, the expenses can be taken out of the benefit that the estate received.

c. *Classifying Nonquantifiable Benefits as Tangible and Acceptable for Administrative Expenses Leaves Discretion to Judges While Still Implementing This Change*

Another solution would be to classify these indirect benefits as quantifiable and allow the judicial branch to sort out which benefits qualify. This shifts the burden to the court and may require some additional time and effort to be invested, but the resulting increase in judicial efficiency across the board will negate the impact of making these determinations.

If codified into a statute, the language may look like this:

(1) In a proceeding where at least one interested party may not recover the full value of its claim, an applicant will be presumed to have made a tangible benefit to the estate if:

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<sup>191</sup> Stone, *supra* note 23, at 223.

<sup>192</sup> Trs. of the Int'l Improvement Fund v. Greenough, 105 U.S. 527 (1881).

<sup>193</sup> Stone, *supra* note 23, at 238 (citing Trs. of the Int'l Improvement Fund, 105 U.S. 527).

<sup>194</sup> *Id.* at 238–39 (citing Trs. of the Int'l Improvement Fund, 105 U.S. at 532).

(A) The applicant benefited the estate in a manner that cannot be quantified but nonetheless conferred a benefit that is greater than the expenses they seek.

*d. Placing the Burden of Showing that a Benefit Is Worthy of Administrative Expenses on the Applicant Would Require Making Room for Them to Make This Argument*

This change would need carve out room for an applicant to demonstrate that their benefit indirectly made a quantifiable contribution to the estate. Currently, this argument is falling upon deaf ears in all circuits and statutory language would be a powerful way to address it.<sup>195</sup> The effort required would fall upon both the applicant to prepare this argument and the courts to make the determination, but the resulting increase in efficiency is worth it. A showing that an applicant contributed to the estate in a way that is not quantifiable but nevertheless made a tangible benefit would create a presumption of a substantial contribution.

The language may look like this:

(1) In a proceeding where at least one interested party may not recover the full value of its claim, an applicant will be presumed to have made a tangible benefit to the estate if:

(A) The Applicant can affirmatively show that they benefited the estate in a manner that cannot be quantified but nonetheless substantially contributed to the estate.

It is important that this language is drafted carefully. Administrative expenses must retain their narrow scope and must not be granted in many situations. This language is not designed to be a loophole, but a narrow exception that allows for applicants, that truly benefited the estate, to recover their costs. Unfortunately, amending the Code may not be the top priority for legislators and so the judicial branch will have to continue using its discretion to implement the best methods.

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<sup>195</sup> *Id.* at 223.



*e. Changing the Judicial Interpretation of the Section 503(B)(3)(D) Analysis Is a Simple and Easy Change That Will Result in the Benefits Listed Above*

This Comment serves as a direct call to the federal judiciary to change the interpretation of the current substantial contribution analysis. Below are potential means for how this could be achieved using the court's § 105 power.<sup>196</sup>

*f. Judges Do Not Have to Conduct a Different Substantial Contribution to Change the Interpretation of Section 503(B)(3)(D) as Proposed*

Although administrative expenses are rarely granted to applicants and are almost never granted to applicants who cannot demonstrate a quantifiable benefit to the estate, the language of the statute nor the test itself are causing these rejections. The requests of applicants are simply falling upon deaf ears.<sup>197</sup> Judges are refusing to grant recovery when there is no quantifiable benefit because they interpret that as failing the tangible benefit requirement. Not only is this requirement judge-made law that could easily be changed, the requirement itself does not imply that a quantifiable benefit must be shown.

Judges across the country could easily change their interpretation without causing any major problems in bankruptcy proceedings. All other requirements that make administrative expenses rare will remain in effect, but those who deserve recovery would have more of an opportunity.

*g. Section 105 of the Bankruptcy Code Allows a Judge the Authority to Implement This Change in Interpretation*

Judges have the authority to invoke § 105 power to “issue any order, process, or judgment that is necessary or appropriate to carry out [the Code’s] provisions.”<sup>198</sup> This section serves to allow judges flexibility to carry out the provisions of the Code, subject to some limitations. Section 105 can only be invoked when necessary to “preserve an identifiable right conferred elsewhere in [the Code.]”<sup>199</sup> Additionally, a bankruptcy judge may not use § 105 to “contravene specific statutory provisions.”<sup>200</sup>

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<sup>196</sup> See 11 U.S.C. § 105(a) (2019) (“The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title.”).

<sup>197</sup> Stone, *supra* note 23, at 223.

<sup>198</sup> 11 U.S.C. § 105(a) (2019).

<sup>199</sup> *In re Jamo*, 283 F.3d 392, 403 (1st Cir. 2002) (citing *Norwest Bank Worthington v. Ahlers*, 485 U.S. 197, 206, (1988); *In re Ludlow Hosp. Soc’y, Inc.*, 124 F.3d 22, 27 (1st Cir. 1997)).

<sup>200</sup> *Law v. Siegel*, 571 U.S. 415, 421 (2014).

Section 105 authority can be used to interpret the substantial contribution requirement as allowing nonquantifiable benefits so long as there is an identifiable right<sup>201</sup> and the action does not contravene any specific statutory authority.<sup>202</sup>

There is an identifiable right in recovery for applicants who have conferred a substantial contribution to the estate under § 503(b)(3)(D). There is no statutory authority stating substantial contributions must be quantifiable for recovery.

*h. Amending the Language of Section 503(B)(3)(D) Is the Most Direct Method of Implementing the Proposed Change*

As § 503(b)(3)(D) is written ambiguously, there is room for Congress to clarify when administrative expenses should be granted. Implementing a change that furthers both of the twin aims of bankruptcy recognized should receive bipartisan support.

*i. Prescribing Specific Benefits That Qualify Ensures Certainty to Applicants and Requires No Extra Effort From Judges*

Implementing a change in the text of § 503(b)(3)(D) that leaves the core of the language intact while adding a provision that lays out specific benefits that qualify as administrative is one possible solution. This change would make applicants aware of which efforts are worth pursuing and which would not result in administrative expenses and require no interpretation from any party to enforce.

This language may look like this:

(1) In a proceeding where at least one interested party may not recover the full value of its claim, an applicant will be presumed to have made a tangible benefit to the estate if,

- (A) The applicant benefited the estate by
  - a. reducing costs to the estate,
  - b. shortening the time of the proceedings,
  - c. maximizing the value of assets,
  - d. proposing a reorganization plan,
  - e. (etc.)

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<sup>201</sup> *In re Jamo*, 283 F.3d at 403 (citing *Norwest Bank Worthington*, 485 U.S. at 206; *In re Ludlow Hosp. Soc'y, Inc.*, 124 F.3d at 27).

<sup>202</sup> *Law*, 571 U.S. at 421.

Congress can also use the language from § 330(a) of the Bankruptcy Code that entitles a debtor to reasonable compensation for actual and necessary services. Section 330(a) provides:

. . . the court may award to a trustee, to an examiner, to a professional person employed under section 327 or 1103 of this title, or to the debtor's attorney—

- (1) reasonable compensation for actual, necessary services rendered by such trustee, examiner, professional person, or attorney, as the case may be, and by any paraprofessional persons employed by such trustee, professional person, or attorney, as the case may be, based on the time, the nature, the extent, and the value of such services and the cost of comparable services other than in a case under this title; and
- (2) reimbursement for actual, necessary expenses.

As written, this language is too broad to be implemented for applicants besides debtors, but it can provide a model for what the updated language should look like.

The language could be tightened up to provide applicants more room to show a substantial contribution without allowing them the same means as a debtor.

. . . the court may award to a creditor, an indenture trustee, an equity security holder, or a committee representing creditors or equity security holders—

- (1) reasonable compensation for a substantial contribution conferred upon the estate, based on the time, the nature, the extent, and the value of such services and the cost of comparable services other than in a case under this title; and
- (2) reimbursement equal to the value added to the estate.

## CONCLUSION

The changes required to allow applicants to recover for nonquantifiable benefits under § 503(b)(3)(D) are easy to implement and worth the effort. Applicants should be given a reasonable opportunity to participate in bankruptcy proceedings to which they have an interest without fearing that they will be

throwing money away without hope of reimbursement. It is the hope of this Comment that reasonable change will be made to thaw the chilling effect of the § 503 administrative expense analysis.

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